

**Statement of Susan Gaffney, Inspector General
U.S. Department of Housing and Urban Development
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Before the Senate Subcommittee on Housing and Transportation**

**THE OFFICE OF INSPECTOR GENERAL'S PERSPECTIVE
ON CHALLENGES CONFRONTING HUD**

Chairman Allard, Ranking Member Reed, and Subcommittee members, I appreciate the opportunity to appear before you today to discuss challenges confronting HUD in the areas of mission and programs, organizational structure, and management operations.

HUD's Mission and Programs

HUD is the principal federal agency responsible for programs concerned with housing needs, fair housing, and improving and developing the Nation's communities. It has a fiduciary responsibility over a multi-billion dollar housing business and a social mission to assist in serving the housing needs of millions of low and moderate-income families. Indeed, HUD's mission is multifaceted and complex. For a relatively small agency of about 9500 staff, it has a lot of work to do. The National Academy of Public Administration's report on HUD in 1994 summed it up well. "Because of the mismatch of goals and resources and its many communities of users, HUD faces a tandem *performance deficit* (the gap between what HUD is supposed to do and has the ability to accomplish) and *expectations glut* (unrealistic perceptions of what HUD can accomplish). The result is a prescription for problems."

Four years ago I testified before the Congress about the importance of coming to a definition of HUD's mission that bears some reasonable relationship to HUD's capability to meet that mission. The revised mission statement must then be used as a springboard for a major streamlining of HUD programs and activities. We must also come to an understanding that HUD staff cannot be all things to all people. We owe HUD employees a clear definition of their roles with respect to policy development, providing technical assistance, motivating the community, overseeing program implementation, and taking enforcement action for inadequate performance.

In 1994, the Office of Inspector General (OIG) counted 240 separate HUD programs and activities. With new programs and activities added since 1994, that number is approaching 300. More often than not, when new HUD programs or activities have been announced, staff resources have not been discussed or considered. But it takes staff and resources to assure that programs are designed properly and that programs include proper checks and balances. Without the proper internal controls and oversight, new programs can, of course, be abused. We've observed this recently with the Officer Next Door Program. Should HUD be discounting thousands of dollars worth of real estate assets to Police offices without any follow-up mechanism to assure these recipients are meeting their end of the bargain?

HUD's proposed 2002 Budget acknowledges this issue in a statement that "the budget emphasizes...minimizing the number of new initiatives that undermine HUD's capacity to administer its core programs...." Obviously, the OIG believes that the

Administration needs to go much further in tightening HUD's mission statement and streamlining its programs. We also recognize that such an effort would be enormously time-consuming and difficult, requiring the support of HUD's customers as well as the Congress. We recommend the effort, nonetheless, as we believe it is a fundamental requirement for HUD's shedding its "high risk" reputation and better serving its intended beneficiaries.

HUD's Organizational Structure

In the last four years, HUD has changed significantly. The former Secretary's 2020 Management Reform Plan envisioned correcting longstanding HUD problems in areas such as resource allocation, financial management, procurement and information systems, and bringing the skill levels of HUD staff up to par.

These planned reforms involved massive reorganizations that shook up nearly every Departmental component. When the changes started taking place late in 1997, we asked the former Secretary to slow down the process, but our calls went unanswered. The push was on for rapid change. Indeed, that was the advice the Secretary received from various reinvention experts. Unfortunately, at HUD, this meant that organizational and process changes were made before a sound management infrastructure was in place. The organizational/process changes were to be made while establishing the management infrastructure, without the benefit of program consolidation or empowerment and within the context of staff reductions. This was an extraordinarily complicated plan. It has

resulted in many staff resources being moved to new, highly centralized organizational units in the Department such as the Real Estate Assessment Center, the Enforcement Center, the Troubled Agency Recovery Centers, and the Grants Management Center, as well as to the new Community Builder function.

Not surprisingly, given the scope of HUD 2020, OIG audits have noted several serious problems with the changes that have taken place. For example, we've observed that certain newly established centers were not operating as intended—planned workload expectations had been seriously overstated. In other cases, we have found that staffing of new organizational units was inadequate or not trained to perform the work. We have, in addition, questioned whether the Community Builder function is the best use of HUD's limited staff resources.

Over the next months, as a priority matter, Secretary Martinez will need to decide if HUD 2020 organizational changes meet his management needs. Existing performance data will assist his decision-making, but he will also need to consider the types of relationships he seeks within HUD and between HUD and its customers, and how HUD's current organization affects those relationships.

HUD's Management Operations

HUD's proposed 2002 budget states that resolving the following management challenges will be a top Secretarial priority:

- Rationalizing the distribution of staff resources in light of program needs;
- Continuing to improve oversight of the local housing agencies and property owners that administer HUD's housing programs;
- Improving income and rent determinations to reduce subsidy overpayments;
- Insuring recipients' full and timely utilization of HUD funds; and
- Improving FHA internal systems and controls to reduce fraud in FHA programs.

HUD's acknowledgement of these problems and the Secretary's commitment to fix them is good news from the OIG's perspective, as these are—apart from the issue of recipients' full and timely utilization of HUD funds--the same management deficiencies that the OIG has been reporting, in our annual audits of HUD's financial statements, as weaknesses in HUD's internal controls. The not so good news is that these problems have existed for many years, and they have proved to be intractable. Permit me to illustrate the intractability by discussing OIG work in each of the areas of material weakness.

Rationalizing the Distribution of Staff Resources in Light of Program Needs

As noted in HUD's proposed budget, the new Resource Estimation and Allocation System will help the Department to assess where staffing should be increased or decreased to effectively administer its programs. HUD is also working to develop a long-

term staffing strategy to meet the rapid increase in retirements expected over the next several years.

Last year, we completed an assessment of the Department's progress in developing and implementing the Resource Estimation and Allocation System. In October 1999, former Secretary Cuomo conveyed to the Congress that HUD needed a resource management system and that he planned to implement such a system within 18 months. We found that HUD, with the National Academy of Public Administration (NAPA), developed a methodology for resource estimation and allocation. Further, NAPA briefed each Assistant Secretary on the resource estimation and allocation methodology and the impact it would have on their programs. Also, HUD selected a contractor to do the measurement studies at various program offices throughout the Department to determine resource estimate requirements. Despite these plans, our audit found the implementation of the Resource Estimation and Allocation System did not progress with any urgency and only a portion of the contract scope was funded. We are very supportive of Secretary Martinez's commitment to completing this important activity.

Continuing to Improve Oversight of the Local Housing Agencies and Property owners that Administer HUD's Housing Programs

Although the Department recognizes that the physical inspections protocol used to assess public housing and multifamily assisted housing needs further refinement to

ensure consistent and fair results, it plans to continue to assess the physical condition of HUD-assisted housing to ensure that it is decent and safe.

Last year we conducted an audit of the Office of Housing's use of physical inspection assessments generated by HUD's Real Estate Assessment Center (REAC) on multi-family properties insured by the Federal Housing Administration and/or receiving project-based subsidy under the Section 8 program. The purpose of our review was to evaluate actions taken to address and track corrections to the physical deficiencies disclosed through the REAC property inspections. We found that although the Office of Housing utilizes the REAC property inspections within their servicing responsibilities, the report addresses the need for the Office of Housing to reinforce its assurances and improve its processes to strengthen the Department's oversight of its portfolio of insured and subsidized multifamily properties. Specifically, we determined that the Office of Housing does not have the proper assurances that corrective action is completed by the owner to the extent of all the physical deficiencies reported by the property's REAC inspection. This includes assurances that exigent health and safety violations are corrected within the required time frame and that complete property surveys identifying the magnitude of the physical deficiencies are performed. Further, we determined that the Office of Housing could improve the current notification process to field office staff of completed property inspection reports and exigent health and safety violations released by REAC.

Improving Income and Rent Determinations to Reduce Subsidy Overpayments

Subsidy overpayments are a problem that has plagued the Department for more than 20 years. Since HUD serves such a small portion of those in need of housing assistance, every dollar needs to be spent properly. HUD provides housing assistance funds under various grant and subsidy programs to multifamily project owners (both nonprofits and for profit) and Housing Authorities (HAs). These intermediaries, in-turn, provide housing assistance to benefit primarily low-income households. HUD spent about \$19 billion in fiscal year 2000 to provide rent and operating subsidies that benefited over 4 million households. Weaknesses exist in HUD's control structure such that HUD cannot be assured that these funds are expended in accordance with the laws and regulations authorizing the grant and subsidy programs. HUD overpays hundreds of millions of dollars in low-income rent subsidies due to the incomplete reporting of tenant income, the improper calculation of tenant rent contributions, and the failure to fully collect all outstanding rent. We've reported this as a material weakness in our annual financial audit since we began this reporting process in 1991.

A recently completed contracted study of rent determinations under HUD's major housing assistance programs estimates that substantial errors are made by project owners and HAs. The study projected that annually, about \$1.9 billion in subsidies was overpaid on behalf of households paying too little rent and about \$0.7 billion in subsidies was underpaid on behalf of households paying too much rent based on HUD requirements. In response to this high incidence of error, HUD's proposed budget commits to

implementing a number of measures to resolve this problem, including the development of tools to assist housing agencies and assisted housing owners in the determination of income and calculation of rent and the introduction of a quality control program to monitor the performance of these intermediaries. HUD also plans to review the current laws and regulations regarding income and rent determinations to ascertain whether their simplification would facilitate program compliance. This constitutes a broader scope approach than previous income matching efforts, and we believe that the broader scope approach makes sense.

Improving FHA Internal Systems and Controls to Reduce Fraud in FHA Programs

HUD's proposed budget recognizes the need to strengthen the integrity of FHA internal systems and controls to reduce fraud in FHA programs. Promised actions include improving the loan origination process and providing better monitoring of lenders and appraisers.

In the last few years, the OIG audit and investigative staffs have been actively involved in examining many aspects of the FHA single-family operations. We've identified rampant origination frauds, property flipping scams, and scandals in the sale of HUD owned properties. Needless to say, all these problems have an impact on the soundness of FHA's Mutual Mortgage Insurance Fund. There are many factors beyond HUD's control—such as interest rates and unemployment rates--that affect the soundness of the MMI Fund. But assuring that programs are run efficiently and effectively and that

programs are sufficiently managed to minimize the opportunities for fraud and abuse is within HUD's control. The Secretary's commitments to making improvements in this area are important to the financial health of the FHA program.

We have performed numerous audits of FHA operations in the last two years including a comprehensive audit of loan origination activity and a nationwide review of Property Disposition Operations. FHA Single Family program personnel are in the process of taking corrective actions on most of our audit recommendations. We appreciate the Secretary's commitment to continuing these actions.

Recognizing that HUD's single family staff have been through downsizing, reorganization, and heightened workload expectations, we need to step back and figure out how we can make the internal control requirements that are on HUD's books actually work to prevent fraud and abuse. Internal controls will not work without sufficiently trained staff to assure that checks and balances are in place. If the Congress and the Secretary of HUD send a clear message that that's what they really want, then I am confident that the single-family staff will be able to figure out how to do it.

Mr. Chairman, that concludes my testimony, I appreciate the opportunity you have afforded me to appear here today.